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Supreme Court, U.S.
FILED
07 1334 APR 22 2008
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No. 07-

IN THE
Supreme Court of the United States

IMPROV WEST ASSOCIATES and
CALIFORNIA COMEDY, INC.,

Petitioners,

v.

COMEDY CLUB, INC. and
AL COPELAND INVESTMENTS,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The Ninth Circuit vacated an arbitration award, which was based upon a good faith and reasoned analysis of state law, on the non-statutory ground that the award was in "manifest disregard of the law." Subsequently, in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. ____, No. 06-989, slip op. 1-15 (March 25, 2008), this Court held that the statutory grounds for vacating, modifying, or correcting an arbitration award specified in the Federal Arbitration Act, 9 U.S.C. §§ 10 and 11, are exclusive and that no non-statutory grounds for vacatur exist. This petition presents the following questions:

1. Whether the Ninth Circuit's decision vacating an arbitration award on the non-statutory ground of "manifest disregard" is inconsistent with this Court's subsequent decision in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. ___, No. 06-989, slip op. 1-15 (March 25, 2008).

2. Whether an arbitrator's good faith but, in the view of the reviewing court, erroneous interpretation of state law constitutes a basis for vacating an arbitration award under the Federal Arbitration Act, 9 U.S.C. §§ 10 and 11.

CORPORATE DISCLOSURE STATEMENT

The Petitioners, Improv West Associates and California Comedy, Inc., have no parent corporations, and no publicly held company owns 10% or more of their stock.

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PETITION FOR WRIT OF CERTIORARI

Petitioners Improv West Associates and California Comedy, Inc. petition this Court for a Writ of Certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in this case on September 7, 2007. The Ninth Circuit denied the Petitioners' petition for rehearing and rehearing *en banc* on January 23, 2008.

OPINIONS BELOW

The Arbitrator's Order Re Motions for Summary Adjudication is reprinted at Petitioners' Appendix I. The Arbitrator's Opinion denying the Respondents' motion for reconsideration is reprinted at Petitioners' Appendix H.

The District Court's Order Confirming Arbitration Award, dated April 12, 2005, is reprinted at Petitioners' Appendix C.

The published opinion of the United States Court of Appeals for the Ninth Circuit affirming in part, vacating in part, and remanding to the District Court for further proceedings, dated September 7, 2007, is reprinted at Petitioners' Appendix B.

The published amended opinion of the United States Court of Appeals for the Ninth Circuit affirming in part, vacating in part, and remanding to the District Court for further proceedings, dated January 23, 2008, is reprinted at Petitioners' Appendix A.

JURISDICTION

The United States Court of Appeals for the Ninth Circuit entered judgment on September 7, 2007, and denied the Petitioners' petition for rehearing and rehearing *en banc* on January 23, 2008. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The Federal Arbitration Act, 9 U.S.C. §§ 9-11, provides:

> § 9. Award of arbitrators; confirmation; jurisdiction; procedure
>
> If the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration, and shall specify the court, then at any time within one year after the award is made any party to the arbitration may apply to the court so specified for an order confirming the award, and thereupon the court must grant such an order unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title. If no court is specified in the agreement of the parties, then such application may be made to the United States court in and for the district within which such award was made. Notice of the application shall be served upon the adverse party, and thereupon the court shall have jurisdiction of such party as though he had appeared generally in the proceeding. If the adverse

party is a resident of the district within which the award was made, such service shall be made upon the adverse party or his attorney as prescribed by law for service of notice of motion in an action in the same court. If the adverse party shall be a nonresident, then the notice of the application shall be served by the marshal of any district within which the adverse party may be found in like manner as other process of the court.

§ 10. Same; vacation; grounds; rehearing

(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration—

(1) where the award was procured by corruption, fraud, or undue means;

(2) where there was evident partiality or corruption in the arbitrators, or either of them;

(3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or

(4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite

award upon the subject matter submitted was not made.

(b) If an award is vacated and the time within which the agreement required the award to be made has not expired, the court may, in its discretion, direct a rehearing by the arbitrators.

(c) The United States district court for the district wherein an award was made that was issued pursuant to section 580 of title 5 may make an order vacating the award upon the application of a person, other than a party to the arbitration, who is adversely affected or aggrieved by the award, if the use of arbitration or the award is clearly inconsistent with the factors set forth in section 572 of title 5.

§ 11. Same; modification or correction; grounds; order

In either of the following cases the United States court in and for the district wherein the award was made may make an order modifying or correcting the award upon the application of any party to the arbitration—

(a) Where there was an evident material miscalculation of figures or an evident material mistake in the description of any person, thing, or property referred to in the award.

(b) Where the arbitrators have awarded upon a matter not submitted to them, unless it is a matter not affecting the merits of the decision upon the matter submitted.

(c) Where the award is imperfect in matter of form not affecting the merits of the controversy.

The order may modify and correct the award, so as to effect the intent thereof and promote justice between the parties.

STATEMENT OF THE CASE

The District Court in the instant case confirmed an arbitration award that was based on the arbitrator's good faith and reasoned application of state law. The Ninth Circuit held that the arbitrator's reasoning was "fundamentally incorrect" and vacated in part the District Court's order on the non-statutory ground of "manifest disregard of the law." The Ninth Circuit's decision conflicts with this Court's subsequent ruling in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. ____, No. 06-989, slip op. 1-15 (March 25, 2008), in which this Court held that the statutory grounds for vacating, modifying, or correcting an arbitration award specified in the Federal Arbitration Act ("FAA"), 9 U.S.C. §§ 10 and 11, are exclusive and that no non-statutory grounds for vacatur exist. Furthermore, irrespective of this Court's holding in *Hall Street*, the Ninth Circuit's decision conflicts with the decisions of this Court and of every other circuit in holding that an arbitrator's

good faith but erroneous interpretation of state law is a ground for vacatur under the FAA.

The Petitioners and the Respondents are parties to a Trademark License Agreement dated June 13, 1999 (the "Agreement") pursuant to which the Petitioners granted the Respondents a license to use the Petitioners' "IMPROV" and "IMPROVISATION" trademarks, along with related trade dress and trade secrets, in connection with comedy club franchises across the country through May 13, 2019. The Agreement contains a covenant against competition that restrains the Respondents from operating competing comedy clubs during the term of the Agreement.

A number of disputes arose between the parties that were collectively submitted to mandatory arbitration under the Agreement. One of those disputes was a challenge by Respondents to the enforceability under California Business and Professions Code § 16600 ("CBPC § 16600") of the covenant not to compete. The arbitrator issued two reasoned orders in which he carefully considered CBPC § 16600 and the California and out-of-state cases applying the statute and determined that the Agreement's in-term covenant not to compete was enforceable under those authorities. App. 104a–110a.

The District Court confirmed the arbitration award by an order dated August 29, 2005. App. 77a–78a. The jurisdiction of the District Court was based on 28 U.S.C. § 1332.

On appeal, the United States Court of Appeals for the Ninth Circuit held that "the arbitrator's

ruling that [the covenant] is a valid covenant not to compete ignores CBPC § 16600 and thus is in manifest disregard of the law." App. 27a. The Ninth Circuit acknowledged that the arbitrator had considered and analyzed both CBPC § 16600 and the applicable case law but held that the arbitrator's interpretation of those authorities was "fundamentally incorrect." *Id.* The Ninth Circuit determined that the arbitrator's good faith but, in its view, erroneous application of state law constituted "manifest disregard," which, under Ninth Circuit law, presented a non-statutory basis for vacating the award. App. 29a.[1]

REASONS FOR GRANTING THE PETITION

I. THE NINTH CIRCUIT'S DECISION WAS ISSUED PRIOR TO, AND APPLIES A STANDARD INCONSISTENT WITH, THIS COURT'S DECISION IN *HALL STREET ASSOC., L.L.C. v. MATTEL, INC.*

This petition should be granted and the case remanded because the Ninth Circuit's decision conflicts with this Court's recent decision in *Hall Street Assoc., L.L.C. v. Mattel, Inc.*, 552 U.S. ___, No. 06-989, slip op. 1-15 (March 25, 2008). *See* Rules of the Supreme Court of the United States, Rule 10(c).

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[1] In a separate part of its decision, the Ninth Circuit held that the arbitrator had exceeded the scope of his authority solely by extending an injunction to reach certain non-parties and directed the District Court on remand to modify the injunction to exclude those non-parties. App. 13a-17a. Petitioners do not challenge that part of the Ninth Circuit's decision in this petition.

The instant case was decided before *Hall Street*. As of that time, the Ninth Circuit recognized "a non-statutory escape valve from an arbitral award where the arbitrator has manifestly disregarded the law." *Luong v. Circuit City Stores, Inc.*, 368 F.3d 1109, 1112 (9th Cir. 2004).[2] The Ninth Circuit availed itself of that non-statutory escape valve in this case, holding that the arbitrator's "fundamentally incorrect" understanding of CBPC § 16600 constituted "manifest disregard" requiring vacatur. App. 27a.

In *Hall Street*, this Court held that the statutory grounds for vacating, modifying, or correcting an arbitration award specified in the FAA, 9 U.S.C. §§ 10 and 11, are exclusive and that no non-statutory grounds for vacatur exist. The Ninth Circuit's decision in the present case therefore conflicts with this Court's decision in *Hall Street*, and the decision should be vacated and remanded for reconsideration in light of *Hall Street*.

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[2] Prior to *Luong*, the Ninth Circuit had suggested that section 10(a)(4) of the Federal Arbitration Act might encompass situations where the arbitrator acted "in manifest disregard of the law." *See Kyocera Corp. v. Prudential-Bache Trade Services, Inc.*, 341 F.3d 987, 1002 (9th Cir. 2003); *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056, 1059-60 (9th Cir. 1991). However, in *Luong*, the Ninth Circuit determined that manifest disregard was a "non-statutory escape valve" from sections 10 and 11 of the FAA rather than a statutory ground for vacatur. *Luong*, 368 F.3d at 1112.

II. THE NINTH CIRCUIT'S HOLDING THAT AN ARBITRATOR'S GOOD FAITH BUT ERRONEOUS APPLICATION OF STATE LAW IS A GROUND FOR VACATUR UNDER THE FEDERAL ARBITRATION ACT CONFLICTS WITH THIS COURT'S DECISIONS AND THE LAW OF EVERY OTHER CIRCUIT.

In holding that an arbitrator's good faith but, in the view of the reviewing court, erroneous interpretation of state law constitutes a ground for vacatur, the Ninth Circuit's decision conflicts with the decisions of this Court and of every other circuit applying the FAA and, if permitted to stand, will open the floodgates for plenary review of arbitration awards based on mere errors of law.

The arbitrator in this case considered and rejected the Respondent's challenge to the Agreement's non-compete covenant in a reasoned decision. The arbitrator ruled that the covenant did not unlawfully restrain the Respondents from engaging in an entire trade or profession because it operated only during the term of the Agreement. Pertinent portions of the arbitrator's analysis are quoted below:

> ... Although the language of Section 16600 is broad in scope, court decisions have upheld agreements limiting competition in a variety of contexts. For example, it has been held that Section 16600 applies only to covenants preventing one from engaging in an *entire* business, trade or profession." Campbell

v. Board of Trustees of Stanford University, 817 F.2d 499, 502 (9th Cir. 1987). And covenants not to compete *during the term* of an employment agreement or distribution contract are regularly upheld. Shaklee U.S., Inc. v. Giddens, 1991 U.S. App. LEXIS 11617, *8-9 (9th Cir. 1991).

...

The authorities cited by the parties support the enforceability of in-term covenants not to compete. Such covenants have been held enforceable during the terms of employment[] agreements, Fowler v. Varian Assoc's Inc., 196 Cal. App. 3d 34, 44 (1987), supplier-distributor arrangements, Keating v. Baskin-Robbins, USA, Co., 2001 WL 407017 (E.D.N.C.) (applying California law) and Great Frame-Up Systems, Inc. v. Jazayeri Enterprises, Inc., 789 F. Supp. 253 (E.D. Ill. 1992) (applying California law). Although the reasoning in these decisions is sparse, they do emphasize that in-term restrictions are only "partial" restraints on competition, because the restrained party (whether employee, distributor, or franchisee) may continue to engage in the relevant business during the term of his or her agreement with the employer, supplier or franchisor. Respondent has not cited any decision invalidating in-term covenants not to compete under Section 16600. The arbitrator finds, therefore,

> that paragraph 9.j of the Agreement is a valid and enforceable in-term covenant under California law.

App. 105a, 108a.

In confirming the arbitration award, the District Court acknowledged that the arbitrator had "spent several pages explaining its position with regards to the non-compete clause" and also that the arbitrator's ruling "finds support in the case law," including both California and out-of-state cases applying CBPC § 16600. App. 72a-73a. The Ninth Circuit nonetheless vacated in part the District Court's order confirming the award, holding that the arbitrator's ruling "ignore[d]" CBPC § 16600 and was therefore "in manifest disregard of the law." App 27a.

The Ninth Circuit's holding that an arbitrator's good faith but, in its view, erroneous application of state law requires vacatur of an arbitration award conflicts with this Court's decisions and the law of every circuit. As this Court explained in *Hall Street*, sections 10 and 11 of the FAA address "egregious departures from the parties' agreed-upon arbitration" such as "corruption," "fraud," "evident partiality," "misconduct," and "misbehavior." *Hall Street*, 552 U.S. at __, slip op. at 9. This Court has contrasted these "specific instances of outrageous conduct" with "review for just any legal error," observing that "[f]raud and a mistake of law are not cut from the same cloth." *Id.*, slip op. at 9-10.

Every Court of Appeals has carefully distinguished between a good faith error of law, which is never a basis for vacating an arbitration award, and deliberate defiance of the law. As the Eight Circuit explained in *Lincoln Nat'l Life Ins. Co. v. Payne*, 374 F.3d 672, 674 (8th Cir. 2004):

> Manifest disregard requires something more than a mere error of law. If an arbitrator, for example, stated the law, acknowledged that he was rendering a decision contrary to law, and said that he was doing so because he thought the law unfair, that would be an instance of 'manifest disregard.' ... To require anything less would threaten to subvert the arbitral process.

Advest, Inc. v. McCarthy, 914 F.2d 6, 10 (**1st Cir.** 1990) ("'[D]isregard' implies that the arbitrators appreciated the existence of a governing legal rule but willfully decided not to apply it."); *Wallace v. Buttar*, 378 F.3d 182, 190 (**2d Cir.** 2004) ("A federal court cannot vacate an arbitral award merely because it is convinced that the arbitration panel made the wrong call on the law."); *Local 863 Int'l Bhd. of Teamsters v. Jersey Coast Egg Producers, Inc.*, 773 F.2d 530, 533 (**3d Cir.** 1985) ("An award may be set aside only in limited circumstances, for example, where the arbitrator's decision evidences manifest disregard for the law rather than an erroneous interpretation of the law."); *Remmy v. PaineWebber, Inc.*, 32 F.3d 143, 149 (**4th Cir.** 1994) ("[A] court's belief that an arbitrator misapplied the law will not justify vacation of an arbitral award.

Rather, appellant is required to show that the arbitrators were aware of the law, understood it correctly, found it applicable to the case before them, and yet chose to ignore it in propounding their decision."); *Brabham v. A.G. Edwards & Sons Inc.*, 376 F.3d 377, 381 (**5th Cir.** 2004) ("Manifest disregard means more than error or misunderstanding with respect to the law.") (internal quotation marks omitted); *Merrill Lynch, Pierce, Fenner & Smith v. Jaros*, 70 F.3d 418, 421 (**6th Cir.** 1995) ("This court has emphasized that manifest disregard of the law is a very narrow standard of review. A mere error in interpretation or application of the law is insufficient.") (internal citation omitted); *Butler Mfg. Co. v. United Steelworkers of Am.*, 336 F.3d 629, 636 (**7th Cir.** 2003) ("[A]n arbitral decision is in manifest disregard of the law only when the arbitrator's award actually orders the parties to violate the law. That the arbitrator in this case may have misunderstood the [governing statute] is simply not relevant.") (internal citation omitted); *Stroh Container Co. v. Delphi Indus., Inc.*, 783 F.2d 743, 750 (**8th Cir.** 1986) (manifest disregard "may be found when arbitrators understand and correctly state the law, but proceed to disregard the same"); *Bowen v. Amoco Pipeline Co.*, 254 F.3d 925, 932 (**10th Cir.** 2001) ("Requiring more than error or misunderstanding of the law, a finding of manifest disregard means the record will show the arbitrators knew the law and explicitly disregarded it.") (internal citation omitted); *Aldred v. Avis Rent-A-Car*, No. 06-14883, 2007 WL 2110720, at *2 (**11th Cir.** July 24, 2007) ("An arbitrator manifestly disregards the law if he was conscious of the law and

deliberately ignored it; merely misinterpreting, misstating, or misapplying the law does not suffice."); *Kanuth v. Prescott, Ball & Turben, Inc.*, 949 F.2d 1175, 1182 (D.C. Cir. 1991) ("'Manifest disregard' may be found, for example, if the panel understood and correctly stated the law but then proceeded to ignore it."). Thus, the focus in every circuit is not on whether the arbitrator got the law right or wrong, but instead on whether he or she made a good faith effort to correctly apply the law.

The Ninth Circuit's decision in this case dramatically alters this "manifest disregard" standard for review of an arbitration award. Whether or not the arbitrator misinterpreted CBPC § 16600 and the cases arising thereunder, it is abundantly clear that he neither ignored nor acted in deliberate defiance of California law. The arbitrator's written orders devoted several pages to a discussion of CBPC § 16600 and its application to the facts of this case. The Ninth Circuit's belief that the arbitrator was wrong is not a ground for vacatur under sections 10 and 11 of the FAA.

CONCLUSION

The Ninth Circuit's decision vacating in part an arbitration award based on the non-statutory ground of "manifest disregard" is inconsistent with this Court's subsequent decision in *Hall Street*. Furthermore, the Ninth Circuit's holding that an arbitrator's good faith but erroneous application of state law is a basis for vacatur under the Federal Arbitration Act conflicts with the uniform precedent of every other circuit.

This Court should grant certiorari, vacate the decision of the Ninth Circuit, and remand this case for further consideration in light of *Hall Street*.

Respectfully submitted,

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